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**THE NEW DEVELOPMENTALISM AND  
CONVENTIONAL ORTHODOXY**

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# THE NEW DEVELOPMENTALISM AND CONVENTIONAL ORTHODOXY

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## RESUMO

O fracasso das políticas e reformas propostas por Washington e Nova York, aqui denominadas “ortodoxia convencional”, em promover a estabilização e o crescimento econômico na América Latina abriu espaço para o surgimento de uma estratégia nacional de crescimento, a qual chamamos “novo-desenvolvimentismo”. Capitalismo, desenvolvimento econômico, nação e estado-nação são conceitos históricos interdependentes. O desenvolvimento do capitalismo depende de uma estratégia nacional que precisa de uma nação capaz de formulá-la. O antigo desenvolvimentismo promoveu o crescimento na América Latina desde os anos 1930, mas nos anos 1980 ficou ultrapassado. Diferentemente, o novo desenvolvimentismo é orientado para as exportações e rejeita o protecionismo. Ambicionando um mercado e um estado fortes, apóia uma disciplina fiscal que vise uma poupança pública positiva. É nacionalista, porque visa o interesse nacional e rejeita as pressões vindas do Norte, mas é um nacionalismo liberal, social e republicano. Diverge fortemente da ortodoxia convencional, porque rejeita a estratégia de crescimento com poupança externa e a abertura da conta capital, afirma que a taxa de câmbio pode e deve ser administrada, e que é necessária uma estratégia especial para combater taxa de juro alta e a moeda apreciada que mantêm a economia brasileira instável e semi-estagnada.

## PALAVRAS CHAVES

desenvolvimentismo; ortodoxia; estratégia nacional; crescimento; estabilidade macroeconômica

## CLASSIFICAÇÃO JEL

O (Economic Development, Technological Change, and Growth)

## ABSTRACT

The failure of the neo-liberal policies and reforms, here called ‘conventional orthodoxy’ in promoting macroeconomic stabilization and economic growth in Latin America opened room in each country for the rise of national strategy of growth which we call ‘new developmentalism’. Capitalism, economic development, nation and nation-state are interdependent historical concepts. Capitalist development depends on a national strategy that relies on a nation capable of formulating it. Old developmentalism was an effective strategy in promoting growth in Latin America since the 1930s, but in the 1980s got distorted and surpassed by the facts. Differently from it, new developmentalism is export oriented, rejecting protectionism. Since it wants a strong market and a strong state, it supports fiscal discipline aiming at positive public savings. It is nationalist, because it is oriented to the national interest, and rejects pressures from the North, but it is a liberal, social and republican nationalism. It differs strongly, however, from conventional orthodoxy because rejects the growth strategy with foreign savings and the opening of capital accounts, says that the exchange rate can and should be administered, and believes that in Brazil a special strategy is required to overcome the high interest rate/appreciated currency which maintains the Brazilian economy **unstable**.

## KEY WORDS

developmentalism orthodoxy national strategy growth macroeconomic stability

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After the failure of the neo-liberal policies prescribed by rich nations to promote macroeconomic stability and development, Latin America has become home to a clear movement for rejecting ‘conventional orthodoxy’. Does this mean that today more developed countries, with sounder democracies, should return to the national-developmentalism of the 1950s, which was so successful in promoting development, but eventually became distorted and plunged into a crisis? Or might we consider a ‘new developmentalism’? In this paper, after examining the crisis of the national development strategy that was old developmentalism, I compare the rising new developmentalism with its earlier version, as well as with the set of diagnoses and policies rich nations have prescribed and pushed to developing countries since the neo-liberal ideological wave became prevalent worldwide: conventional orthodoxy. In the first section, I discuss old developmentalism, its initial success, its becoming outdated due to a series of new facts and distortions, and its replacement with conventional orthodoxy since the late 1980s. In the second section I discuss new developmentalism as a ‘third discourse’ lying between the bureaucratic left wing’s populism and the neo-liberalism of conventional orthodoxy. In the third section, I discuss the importance of the concept of nation and of the ‘national development strategy’ institution. In the fourth section, I compare new and old developmentalism. In the fifth, I compare it with conventional orthodoxy. In the sixth section, I complete the comparison, presenting two pairs of alternative policy ‘tripods’: the first pair opposing conventional orthodoxy and new developmentalism on economic growth, and the second, opposing the two strategies on macroeconomic policy.

#### 1.1.1.1 Old developmentalism and its crisis

Between the 1930s and the 1970s, Brazil and the remaining Latin American countries grew at an extraordinary pace. They took advantage of the weakening of the center to formulate national development strategies that, in essence, implied protection of the infant national industry and the forced promotion of savings through the State. This strategy was called ‘developmentalism’, or ‘national-developmentalism’. The purpose of such a name was to emphasize that, first, the

policy's basic objective was to promote economic development, and, second that in order for this to happen, the nation — that is, businessmen, State bureaucracy, middle classes and workers joined together in international competition — needed to define the means to reach this objective within the framework of the capitalist system, with the State as principal collective action instrument. The notable economists that, then, studied development and made economic policy proposals, the politicians, government officials and businessmen that were most directly involved in this process were called 'developmentalists' because they chose development as the ultimate goal for their economic analysis and political action. Latin-American economists who, together with a group of international economists, took part in formulating 'development economics' were affiliated with three complementary schools of thought: the classical economics of Smith and Marx, Keynesian macroeconomics, and the Latin-American structuralist theory.<sup>1</sup> Developmentalism was not an economic theory, but a national development strategy. It employed economic theories to formulate, for each country in the capitalist periphery, a strategy capable of gradually leading to the development level attained by central countries: market-based theories, for there is no economic theory that does not spring from the markets, but also political economy theories that cast the state and its institutions in a leading role as auxiliary coordinator of the economy. Developmentalism faced opposition from neo-classical economists that practiced 'conventional orthodoxy' — that is, the set of diagnoses and economic policies and institutional reforms that rich, or Northern, nations prescribed to developing, or Southern, countries. They were called 'monetarists', due to the emphasis placed on monetary supply as a means to control inflation.

As Brazil was a peripheral or dependent, country, whose industrial revolution was taking place 150 years after England's, and more than 100 after the United States', the remarkable development had between the 1930s and 1970s was only possible inasmuch as Brazil as a nation was able to use its state as an instrument to define and implement a national development strategy

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<sup>1</sup> In Brazil, the two leading economists who contributed to development economics were Celso Furtado and Ignácio Rangel. Given the former's international projection, he was also part of the founding group of development economists, which also included Rosentein-Rodan, Arthur Lewis, Ragnar Nurkse, Gunnar Myrdal, Raúl Prebisch, Hans Singer and Albert Hirschman.

where the State's intervention was significant. This was not about replacing the market with the State, but, rather, about strengthening the State in order to enable it to create the required conditions for firms to invest so that their businessmen could innovate. All, beginning with England itself, required a national development strategy to bring about their industrial revolutions and continue to develop. The use of a national development strategy was particularly evident among late-development countries such as Germany and Japan, which, therefore, were never characterized by dependence. Peripheral countries, on the other hand, like Brazil and other Latin American countries, having lived through the colonial experience, remained ideologically dependent on the center after their formal independence. Both late-development central countries and former colonies needed to formulate national development strategies, but the task was easier for the former. For peripheral countries there was the additional hurdle of facing their own 'dependence', that is, submission of the local elites to those in central countries, who were interested in nothing other than their own development. Developmentalism was the name given to national strategy of dependent countries, those whose industrialization began no earlier than the 1930s, or World War II. Their developmentalism was nationalist because, in order to become industrial, these countries needed to form their national state. The nationalism present in developmentalism was the ideology for forming a national state; it was the affirmation that, in order to develop, countries needed to define their own policies and institutions, their own national development strategy.<sup>2</sup> Although not given the same name, late central countries also used developmentalist strategies, as they were nationalistic, as they always followed their own criteria rather than their competitors' to formulate policies, and as they used their states deliberately to promote development.

In the 1940s, '50s and '60s, developmentalists and Keynesians prevailed in Latin America: they were the mainstream. Governments used their theories first and foremost economic policy-making. From the 1970s, however, in the context of the great neo-liberal,

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<sup>2</sup> Nationalism can also be defined, as Geller did, as the ideology that attempts to endow every nation with a state. Although this is a good definition, it is typical of Central Europe. In Latin America, nations were not yet fully formed and, still, were endowed with states. The nations, however, were incomplete, and their regime was semi-colonial: with independence, the main change was the dominant power, which shifted from Spain or Portugal to England and other major central countries.

conservative wave that began to form, Keynesian theory, development economics and Latin-American structuralism were successfully challenged by neo-classical economists, who adopt a neo-liberal ideology in their majority. Since the 1980s, in the context of the great foreign debt crisis that adds to rich nations' political power, these economists manage to redefine in neo-liberal terms their prescriptions for developing countries. The neo-liberal ideology targeted at these countries becomes hegemonic, expressing itself through what became known as the Washington consensus, but which I prefer to call 'conventional orthodoxy'. In other words, during the 1980s, the national development strategy that was developmentalism faces crisis and is replaced with an outside strategy: conventional orthodoxy.

Several factors help explain this. Because old developmentalism was based on import substitution, it carried the seed of its own demise. Protection of national industry, the focus on the market and the reduction of an economy's openness coefficient, even if a relatively large economy such as Brazil's, is greatly constrained by economies of scale. For certain industries, protection becomes absurd. As a result, when the import-substitution model was maintained through the 1970s, it was leading Latin-American economies to a deep distortion. On the other hand, as Furtado remarked as early as 1966,<sup>3</sup> after the initial import substitution phase at consumer goods industries, continued industrialization implies a substantial increase of the capital-labor ratio, with two consequences: income concentration and reduced capital productivity, or product-capital ratio. The response to income concentration was to be an expanded production of luxury consumer goods, characterizing what I have termed 'industrial underdevelopment model', which, besides being perverse, carries the seed of the dissolution of the national pro-development alliance.

The second reason concerns the dissolution, during the 1960s, of the national alliance that served as political foundation for developmentalism. The national-developmental approach assumed the constitution of a nation in each Latin-American country. A reasonable assumption, as, after a lengthy period of dependence that followed the independence movements of the early 19<sup>th</sup> Century, these countries, since 1930, take advantage of the crisis up North to begin their

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<sup>3</sup> Celso Furtado, *Subdesenvolvimento e Estagnação da América Latina* (1966)

national revolutions. Based on this fact, developmentalism proposed that each country's new industrial businessmen should become a national bourgeoisie, as had been the case in developed countries, and associate itself with government officials and urban workers to bring about a national and industrial revolution. Therefore, in every country the sense of nation, of national society, was reinforced and the possibility dawned that this society might implement a national development strategy (developmentalism), using the state as its instrument for collective action. It was at once a proposal and an assessment of the reality represented by the accelerated industrialization process Latin America was then experiencing. The Cuban revolution of 1959, however, by radicalizing the left-wing, and the economic crisis of the early 1960s, led to the dissolution of the national alliance and set the stage for the establishment of military regimes in Brazil, Argentina, Uruguay and Chile, with support from each country's businessmen and from the United States. As a consequence, that alliance, so essential to the constitution of a nation, breaks up and Latin America's moderate left embraces the theses of the 'theory of associated dependence' which rejected the possibility of a 'national bourgeoisie'. In doing so, it rejected the very idea of nation and of national development strategy on which national-developmentalism was seated. The great crisis of the 1980s — the ultimate crisis endured by the import-substitution model that developmentalism had supported since the 1940s — further weakens it. Since then, developmentalism, still supported by the bureaucratic-populist left wing that formed in the shadow of the state because of the distortions the development strategy suffered, but with no support from businessmen, from the modern left, and from a large portion of the State bureaucracy itself, is gradually prevented from opposing the neo-liberal ideological wave that came from the North.<sup>4</sup>

The third reason for the replacement of developmentalism with conventional orthodoxy lies in the strength of this ideological wave. In the early 1980s, in response to the foreign debt crisis, conventional orthodoxy establishes itself bit by bit. The Baker Plan (1985), so called after US Secretary of the Treasure James Baker, completes the definition of the new ideas by adding market-oriented institutional reforms to orthodox macroeconomic adjustment. Developmentalism

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<sup>4</sup> I analyzed this crisis, which was, in broader terms a state crisis, in Bresser-Pereira (1992) *A Crise do Estado*.

then becomes the target of systematic attack. Taking advantage of the economic crisis that derived, in part, from the overcome development model and from the distortions it had suffered in the hands of populist politicians and middle classes, conventional orthodoxy gives developmentalism a negative connotation, identifying it with populism or irresponsible economic policies. In its stead, it proposes a panacea of orthodox and neo-liberal institutional reforms. It further proposes that developing countries abandon the antiquated concept of 'nation' that national-developmentalism had adopted, and accept the globalist thesis according to which, in the age of globalization, nation-states had lost autonomy and relevance: worldwide free markets (including financial ones) would be charged with promoting the economic development of all.

Twenty years later, what we see is conventional orthodoxy's failure to promote Latin America's economic development. While developmentalism prevailed, between 1950 and 1980, per capita income in Brazil grew almost 4% a year; since then, it grew for times less! The performance of other Latin-American countries was no different, with the exception of Chile. In the same period, however, dynamic Asian countries, including China since the 1980s, and India since the 1990s, kept or achieved extraordinary growth rates.

Why such different growth rates? At the more immediate level of economic policies, the fundamental problem relates to loss of control over the most strategic macroeconomic price in an open economy: the foreign exchange rate. While Latin-American countries lost control over it via open financial accounts and saw their foreign exchange rates appreciate as, from the early 1990s, they accepted the proposal of growth with foreign savings from Washington and New York, Asian countries mostly kept current account surpluses, as well as retained control over their foreign exchange rates. At the reforms level, while Latin-American countries indiscriminately accepted all liberalizing reforms, irresponsibly privatizing monopoly utilities and opening their capital accounts, Asians were more prudent. However, it gradually became clear to me that the main difference was to be found in a new, fundamental fact: Latin-American countries interrupted their national revolutions, watched as their nations disorganized, lost cohesiveness and autonomy and, as a consequence, were left without a national development strategy. The national strategy Latin American countries in general and Brazil in particular adopted between 1930 and 1980 was known as developmentalism. In this period, and mainly from 1930 to 1960, many Latin-

American countries were firmly steadfastly their nations, finally providing their formally independent states with a basic solidarity when it came to competing internationally. But the weakening brought about by the great crisis of the 1980s, combined with the hegemonic force of the ideological wave that began in the United States in the 1970s, caused the constitution of Latin-American nations to interrupt itself and regress. Local elites stopped thinking with their own heads and accepted the advice and pressure from the North, while countries, devoid of a national development strategy, saw their development come to a stall. Conventional orthodoxy, which came to replace national-developmentalism, had not been developed locally; it did not reflect national concerns and interests, but, rather, the visions and objectives of rich nations. In addition, as is typical of the neo-liberal ideology, it was a negative proposal that assumed the markets' ability to coordinate everything automatically, proposing that the state stop playing the economic role it always had in developed countries: that of supplementing the market's coordination to promote economic development and equity.

I have been critical of conventional orthodoxy ever since it became dominant in Latin America. I was, probably, the first Latin-American economist to criticize the Washington Consensus at my keynote lecture during the annual congress of the National Association of Post-Graduate Economics Courses, in 1990.<sup>5</sup> My criticism, however, gained a new dimension since the first quarter of 1999, after four and a half years as a member of the Cardoso administration. Then I wrote, in Oxford, "Incompetência and *confidence building* por trás de 20 anos de quase-estagnação da América Latina".<sup>6</sup> Soon thereafter, resuming by association with Yoshiaki Nakano, who was also fresh out from an experience in government, we co-authored "Uma estratégia de desenvolvimento com estabilidade" and "Crescimento Econômico com Poupança Externa?".<sup>7</sup> Loyal to the original spirit of developmentalism and to our Keynesian and structuralist background, with these works we began a systematic and radically non-populist criticism of the conventional orthodoxy that had become prevalent in Latin America, offering an alternative

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<sup>5</sup> Bresser-Pereira (1990 [1991]) "A crise da América Latina: Consenso de Washington ou crise fiscal?"

<sup>6</sup> Bresser-Pereira (1999[2001]).

<sup>7</sup> Bresser Pereira and Nakano (2002 and 2002 [2003])

economic policy.<sup>8</sup> Our criticism showed that the conventional proposal, albeit inclusive of certain necessary policies and reforms, did not in fact promote a country's development, but kept it semi-stagnant, incapable of competing with wealthier countries, easily falling prey to a form of economic populism: foreign exchange populism.

The alternative economic strategy alternative that is implicitly or explicitly present in these works and others we produced subsequently, in addition to not running into the distortions developmentalism suffered in its latter days, innovated by acknowledging a series of new historical facts that implied a need to review the national development strategy. How to name this alternative? In early 2003, in a conversation with Nakano about this matter, he suggested 'new developmentalism', which I immediately accepted.<sup>9</sup> At the moment I was finishing the fifth edition of *Desenvolvimento e Crise no Brasil*, and, in addition to including the new ideas in its final chapter, "Retomada da revolução nacional e novo desenvolvimentismo", I used the term for the first time in a written work.<sup>10</sup> In 2004 I published an article so titled in the *Folha de S. Paulo* newspaper.<sup>11</sup> That same year, João Sicsú, Luiz Fernando de Paula and Renaut Michel organized the book *Neo-desenvolvimentismo: Um Projeto Nacional de Crescimento com Equidade Social* — gathering some of the new generation's top economists. New developmentalism thus grew from an isolated proposal into a more general project.<sup>12</sup>

What does new developmentalism involve? I introduce it in this work. In the first section, I define it as a 'third discourse' and a national development strategy; in the second section, I

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<sup>8</sup> In fact, we had begun this work in our period in the Ministry of Finance (1987), myself as minister and he as Secretary for Economic Policy. We then went to war against the populist elements within PMDB, while rejecting the mere adoption of the conventional orthodoxy that the IMF and the World Bank then prescribed for Brazil.

<sup>9</sup> We also considered using 'developmentalist orthodoxy', given that new developmentalism is at least as strict as conventional orthodoxy in terms of fiscal discipline. The term 'orthodoxy', however, suggests a lack of flexibility and, therefore, of pragmatism, which is incompatible with a national development strategy.

<sup>10</sup> Bresser-Pereira (2003: Capítulo 20) "Retomada da revolução nacional and novo desenvolvimento".

<sup>11</sup> Bresser-Pereira (2004) "O novo desenvolvimento".

<sup>12</sup> As I write this (early 2006), Sicsú and de Paula have submitted to *Revista de Economia Política* an article titled "Novo Desenvolvimento", still pending peer review. A seminar coordinated by José Luís Oreiro and Luiz Fernando de Paula is set to take place at Universidade Federal do Paraná in 2006, with new developmentalism as topic.

establish its differences from the 1950s' developmentalism; and, in the third section, I show how it stands as a critique and alternative to conventional orthodoxy, that is, to the diagnoses, policies and reforms conceived mainly in Washington for use in developing countries.

#### 1.1.1.2 Nation and nationalism

New developmentalism, as the national-developmentalism of the 1950s, at once assumes the presence and implies the formation of a true nation, capable of formulating an informal, open, national development strategy, as is proper of democratic societies whose economies are coordinated by the market. A nation is a society of individuals or households that, sharing a common political fate, manages to organize itself as a state with sovereignty over a certain territory. A nation, therefore, like the modern state, only makes sense within the nation-state framework that arises with capitalism. For a nation to be able to share a common fate it must have common objectives, chief among which, in historical terms, the objective of development. Other objectives, such as freedom and social justice, are also fundamental to nations, but, like the state and capitalism, arise with economic development as part of its reasoning, of its intrinsic manner of being. Nations, nation-states, capitalism and economic development are simultaneous and intrinsically correlated historical phenomena. In its most developed form — today's globalization — capitalism's economic constituents are not only firms operating at the international level, but also, if not mainly, nation-states or national states. It is not just firms that compete worldwide in the markets, as conventional economic theory proposes: nation-states, too, are fundamental competitors. The main criterion for success for the political rules of every modern nation-states is comparative economic growth. Rulers are successful in the eyes of their people and internationally if they achieve greater growth rates than countries regarded as direct competitors. Globalization is the stage of capitalism where, for the first time, nation-states span the entire globe and compete economically through their firms.

A nation involves a basic solidarity among classes when it comes to competing internationally. Businessmen, workers, state bureaucrats, middle-class professionals and intellectuals may come into conflict, but know they share a common fate, and that this fate relies on their successful competitive involvement in the world of nation-states. It involves, therefore, a

national agreement. A national agreement is the basic social contract that gives rise to a nation and keeps it strong or cohesive; it is the compact among social classes of a modern society that enables this society to become a true nation, that is, a society gifted with a state capable of formulating a national development strategy. The great national agreement or compact that established itself in Brazil since 1930 joined the infant national industrial bourgeoisie to the new bureaucracy or the new state technicians; add to these urban workers and more domestic market-oriented sectors of the old oligarchy, such as the ranchers from which Vargas came. Their adversaries were imperialism, represented mainly by British and American interests, and the affiliated exporting rural oligarchy. The most strategic accord in a modern nation-state is that between industrial businessmen and the State bureaucracy, which includes significant politicians, but also workers and as middle classes. And there will always be domestic adversaries, somehow identified with imperialism or today's colony-less neo-imperialism, as well as with local collaborationist or globalist groups. In the case of Brazil, today, it is rentiers that rely on high interest rates and the financial industry, which collects commissions from the former.

A nation is always nationalist, inasmuch as nationalism is the ideology of the formation of a national state and its permanent reaffirmation or consolidation. Another way to define nationalism is to say, after Ernest Gellner, that it is the ideology that pursues a correspondence between nation and state, that stands for the existence of a state for each nation.<sup>13</sup> This, too, is a good definition, but one typical of a thinker from Central Europe; a definition that becomes exhausted as soon as a nation-state is formed — when nation and state begin coinciding over a given territory, formally establishing a 'sovereign state'. It fails therefore, to take into account Ernest Renan celebrated 1882 sentence: "a nation is a daily referendum".<sup>14</sup> It fails to explain how a nation-state may formally exist in the absence of a true nation, as is the case of Latin-American countries, which, in the early 19th Century, saw themselves endowed with state due not only to

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<sup>13</sup> Gellner, a Czech philosopher who took refuge from communism in England, was probably the most argute analyst of nationalism in the second half of the 20<sup>th</sup> Century: Gellner (1983, 1993).

<sup>14</sup> Ernest Renan (1882 [1992]: 55. In the immediately preceding part, Renan wrote: "A nation is a great solidarity made up of the sentiment of the sacrifices made and those people are still willing to make. It assumes a past; its present summation is a tangible fact: the consent, the clearly expressed desire to go on with common life."

the patriotic efforts of nationalist groups, but also to the good services of England, whose aim was to oust Spain and Portugal from the region. In this way, these countries saw themselves endowed with a state in the absence of true nations, as they ceased to be colonies and became dependent on England, France, and, later, the United States. For a true nation to exist, the several social classes must, despite the conflicts that set them apart, be solidary when it comes to competing internationally, and use national criteria to make policy decisions, particularly those that involve economic policy and institutional reform. In other words, the rulers must think with their own heads instead of dedicating themselves to confidence building, and the entire society must be capable of formulating a national development strategy.

New developmentalism will become a reality when the national society becomes a true nation. This is what happened in Brazil between 1930 and 1980, particularly from 1930 to 1960. Under the rule of Brazil's 20<sup>th</sup> century statesman, Getúlio Vargas, the country took national decisions into its own hands and formulated a successful national development strategy. In those 30 years (or 50, should we include the military period, which remained nationalist, despite its political alliance with the United States against communism), Brazil changed from an agricultural into an industrial country, grew from a mercantilist social formation to a fully capitalist one, from a semi-colonial to a national status. Developmentalism was the name given to the national development strategy and to its driving ideology. Therefore, the process of defining the new developmentalism equally involves resuming the idea of nation in Brazil and other Latin American countries. It implies, therefore, a nationalist perspective in the sense that economic policies and institutions must be formulated and implemented with national interest as their main criterion and with each country's citizens as actors. Such a nationalism aims not to endow a nation with a state, but to turn the existing state into an effective instrument for collective action by the nation, an instrument that enables modern nations, in the early 21<sup>st</sup> Century to consistently pursue their political objectives of economic development, social justice and freedom within an international framework of competition, but also peace and collaboration, among nations. It implies, therefore, that such nationalism be liberal, social and republican, that is, that it incorporate the values of modern industrial societies.

### 1.1.1.3 The 'third discourse' and the national development strategy

New developmentalism is, at once, a 'third discourse' lying between the populist discourse and the discourse of conventional orthodoxy, and the set of diagnoses and ideas that should be the guidelines for each nation-state's national development strategy formulation. It is the set of institutional-reform economic-policy proposals through which medium development nations attempt, in the early twenty-first Century, to catch up with developed countries. Like the old developmentalism, it is not an economic theory: it is based mainly on Keynesian macroeconomics and development economics, but uses a national development strategy. It is the means by which countries like Brazil may successfully compete — and gradually catch up — with rich nations. It is the set of ideas that enables developing nations to refuse rich nations' proposals and pressures for reform and economic policy, like a fully open capital account and growth with foreign savings, inasmuch as such proposals are neo-imperialist attempts to neutralize development — the 'kicking away the ladder' practice. It is the means by which businessmen, government officials, workers and intellectuals can stand as a true nation to promote economic development. I do not include poor countries into the new developmentalism, not because they do not require a national development strategy, but because, still in need to accomplish their primitive accumulation and industrial revolutions, the challenges they face and the strategies they will require are different.

In terms of discourse or ideology, we have, on the one hand, the dominant, imperial and globalist discourse that flows from Washington and is embraced in Latin America by the neo-liberal, cosmopolitan right wing comprised mainly of the rentier class and the financial industry.<sup>15</sup> This is conventional orthodoxy: an ideology exported to developing countries; an anti-national strategy that, despite its generous offer to promote prosperity among medium development countries, in fact serves rich nations' interest in neutralizing these countries' ability to compete. This, as it was applied in Brazil since the 1990s, has four things to say: first, that the country's major problem is the lack of microeconomic reforms capable of enabling the market to

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<sup>15</sup> By 'rentier class' we mean no longer the class of large landowners, but that of inactive capitalists whose livelihood relies mainly on interest income. The 'financial industry', in turn, involves, besides rentiers, businessmen and managers who collect commissions from rentiers.

operate freely; second, that even after the end of runaway inflation, in 1994, controlling inflation remains the main purpose of economic policy; third, that, in order to achieve such control, interest rates must be inevitably high because of the sovereign risk and of fiscal issues; fourth, that ‘development is a great race among countries to obtain foreign savings’, and that the implicit current account deficits and foreign exchange appreciation brought about by capital inflows are no cause for concern. The disastrous effects of this discourse in terms of balance of payments crises and low growth for Latin-American countries that adopted it since the late 1980s are well known today.<sup>16</sup>

The opposite discourse is that of the bureaucratic-populist left wing. From this perspective, Brazil’s ills are due to globalization and financial capital, which placed the country under the burden of high foreign and public indebtedness. The proposed solution was to renegotiate the country’s foreign and public at a great discount. The second ill lied with insufficient demand, which could be resolved with increased public spending. And the greatest ill — unequal income distribution — could be solved by expanding the Brazilian welfare system. This alternative was used, for example, in Peru under Alan Garcia. In Brazil, it was never fully put into practice.<sup>17</sup>

The first discourse served the interests of the North and reflected its deep ideological hegemony over Latin-American countries. Locally, it sprung chiefly from the Brazilian rentier class, who depends essentially in interest for a living, and from economists affiliated with the financial industry; a confused, disoriented upper-middle class also shared it. The second came from the lower-middle class and labor unions, reflecting the old bureaucratic left wing’s perspective. Neither discourse had a chance of reaching a reasonable consensus in Brazilian society, due to their irrationality and biased nature. Neither ideology reflected national interests. Might there be a third discourse capable of achieving such a reasonable consensus? Certainly, this third is possible and is being formulated, little by little. It is the discourse of new

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<sup>16</sup> See Frenkel (2003).

<sup>17</sup> The Workers Party, PT, adopted such discourse in Brazil, but once in power, in 2003, adopted policies recommended by conventional orthodoxy.

developmentalism. But is not new developmentalism also an ideology, as are conventional orthodoxy and the bureaucratic-populist discourse? Yes and no. Yes, because every national strategy implies an ideology — a set of political action-oriented ideas and values. And no, because unlike conventional orthodoxy, which is no more than an outside proposal, new developmentalism will only make sense if it rises from internal consensus and, therefore, stands as a true national development strategy. A full consensus is impossible, but a consensus that brings together businessmen from the production sector, workers, government officials and middle-class professionals — a national agreement, therefore — is now forming, taking advantage of the failure of conventional orthodoxy. This forming consensus regards globalization as neither a blessing nor a curse, but as a system of intense competition among national states through their firms. It realizes that, in such a competition, the State must be strengthened fiscally, administratively and politically, and, at the same time, provide national firms with the conditions to become internationally competitive. It acknowledges, as Argentina has already done after its 2001 crisis, that development in Brazil is prevented, in the short term, by exceedingly high short-term interest rates determined by the Central Bank, which push long-term rates upwards and uncouple them from sovereign risk. It assumes that, for development to occur, investment rates must by necessity rise, and the state must contribute by means of positive public savings, the fruit of curbing current or consumption state expenditures. Finally, and more generally, new developmentalism assumes that development, in addition to being prevented by the absence of democratic nationalism (an absence that favors conventional orthodoxy), is also hampered by income concentration, which, besides unfair, is a culture medium for all forms of populism, and, thus, for the bureaucratic-populist discourse.

What is a national development strategy? More than a simple ideology developed abroad like conventional orthodoxy, it is a set of economic development-oriented institutions and policies. It is less of a national development project or plan because it is not formal, it lacks a document that accurately describes objectives to be attained and policies to be implemented in order to attain such objectives, because the inherent accord among social classes has neither text nor signatures. And it is more, because it informally comprehends all of society, or a large share thereof. Because it shows all a path to tread, and certain very general guidelines to be observed.

Because, although it does not assume a conflict-free society, it does require a reasonable union of all when it comes to competing internationally. Because it is more flexible than a project. Because it always considers the actions of other opponents or competitors. Because the factor that drives individual behavior is not just personal interest, but competition with other nations. A national development strategy reflects all this. Its leadership befalls the government and the more active elements of civil society. Its fundamental instrument is the state itself: its norms, policies and organization. Its outcome, when a major accord establishes itself, when strategy becomes truly national, when society begins sharing, loosely but effectively, methods and goals, is accelerated development — a period during which the country enjoys high per capita income and living standards growth rates.

A national development strategy implies a set of fundamental variables for economic development. These variables are real and institutional alike. The nation's increased savings and investment capacities, the means by which it incorporates technical advances into production, human capital development, increased national social cohesiveness resulting in social capital or in a stronger, more democratic civil society, a macroeconomic policy capable of assuring the state's and the nation-state's financial health, leading to conservative domestic and foreign indebtedness ratios, are all constituents of a national development strategy. In this process, institutions, instead of mere one-size-fits-all abstractions, are seen and construed concretely, historically. A national development strategy will gain meaning and strength when its institutions — be they short-term ones I call policies or public policies, be they relatively permanent ones (institutions proper) — respond to societal needs, when they are compatible with the economy's production factors endowment, or, put more broadly, with the elements that make up society at its structural level.

#### 1.1.1.4 Old and new developmentalism

The developmentalism of the 1950s and the new developmentalism differ based on two variables that arose in this half-century: on the one hand, new historical facts that changed world capitalism, which moved from its 'golden years' to the 'globalization' phase; on the other hand, medium development countries like Brazil changed their own development stages and are no longer marked by infant industries.

The main change at the international level was from the capitalism of the golden years (1945-1975), when the welfare state was assembled and Keynesianism ruled, while development economics prevailed as a theory and a practice of economic development, to the neo-liberal capitalism of globalization, where growth rates are smaller and competition among nation-states is far fiercer. In the golden years, medium development countries still posed no threat to rich nations. Since the 1970s, however, with the NICs (newly industrializing countries), and since the 1990s, with China, their competition becomes much greater: the threat their cheap labor poses rich nations is clearer than ever. At that time, rich nations, and the United States in particular, in need of allies for the Cold War, were far more generous; today, only the poorest African countries can expect some generosity — but even these must be wary, because the treatment rich nations and the World Bank afford them, and the help, or alleged help, they receive are often perverse.

The main difference, at the national level, concerns the fact that industry was in its infancy at that time; it is now mature. The import-substitution model was effective, between the 1930s and the 1960s, to establish the industrial bases of Latin American countries. Since the 1960s, however, they should have begun dropping protectionist barriers and orienting themselves towards an export-led model under which they might show themselves as competitive manufactured goods exporters. They did not, however, until forced to by the crisis of the 1980s, and then often hurriedly and haphazardly. This 20-year lag was one of the greatest distortions endured by the developmentalism of the 1950s.

New developmentalism is not protectionist. It assumes that medium development countries have already overcome the infant industry stage, requiring firms to be competitive in all industries where they operate and to be particularly competitive in some to be able to export. Unlike old developmentalism, which embraced the exporting pessimism of development economics, new developmentalism is not so affected. Like any development strategy, it does not intend to base growth on the export of low value added primary products, but, instead, lays odds on developing countries' ability to export medium value added manufactured goods or high value added primary products. The experience of the past 30 years has clearly shown that this pessimism was one of the great theoretical mistakes of development economics. In the late 1960s,

Latin American countries should have begun shifting decisively from the substituting to the export-led model, as did Korea and Taiwan. In Latin America, Chile was the first to operate such a change and, as a result, its development is often pointed out as an example a successful neo-liberal strategy. In fact, neo-liberalism was only fully practiced in Chile between 1973 and 1981, coming to an end with a major balance of payments crisis in 1982.<sup>18</sup> The export-led model is not specifically neo-liberal because, strictly speaking, the neo-classical economic theory that underlies this ideology has no room for development strategies. Dynamic Asian countries, having adopted a developmentalist strategy in the 1950s, lent it a manufactured goods exporting nature in the 1960s and, since the 1970s at least, can be regarded as neo-developmentalists countries. The export-led model has two main advantages over the imports substitution model. Firstly, the market available to industries is not constrained to the domestic market. This is important for small countries, but equally fundamental to a country with a relatively large domestic market such as Brazil. Secondly, if a country adopts this strategy, economic authorities, making industrial policy in benefit of their firms, get access to an efficiency criterion to guide themselves by: only firms that are efficient enough to export will benefit from the industrial policy. In the case of the import-substitution model, very inefficient firms may be enjoying the benefits of protection; in the case of the export-led model, the likelihood of this happening is substantially smaller.

The fact that the strategy new developmentalism stands for is not protectionist does not mean that countries should be willing to accept indiscriminate openness. They must negotiate pragmatically at the level of the World Trade Organization and regional accords to secure mutual openness. And, above all, it does not mean that the country should give up industrial policies. Room for these has been reduced by the highly unfavorable agreements made in the WTO's Uruguay Round, but there still room for such policies, if considered strategically, in consideration of future comparative advantages that may arise as some supported firms achieve success.

New developmentalism rejects misled notions of growth based chiefly on demand and public deficit that became popular in Latin America in the 1960s. This was one of the most

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<sup>18</sup> See Dias-Alejandro (1981); French-Davis (2003).

severe distortions developmentalism endured in the hands of its populist latter-day advocates. The theoretical roots of this national development strategy lie not in Keynesian macroeconomics and in development economics, which, in turn, is seated mainly on classical economics. Keynes pointed out the importance of aggregate demand and legitimized resorting to public deficits in recessive periods. But he never stood for chronic public deficit. He always assumed that a fiscally balanced national economy might, for a brief while, give up this balance to reestablish employment levels.<sup>19</sup> The notable economists, such as Furtado, Presbisch and Rangel, who formulated the developmentalist strategy, were Keynesian, and, regarded aggregate demand management as an important tool for promoting development. But they never defended the economic populism of chronic deficits. Those that came in their wake, however, did. When Celso Furtado, faced with the severe crisis of the early 1960s, proposed his *Plano Trienal* (1963), these second-class followers accused him of having an ‘orthodox rebound’. In fact, what Furtado already saw and the new developmentalism firmly defends, is fiscal balance. New developmentalism defends it not due to ‘orthodoxy’, but because of the realization that the state is the nation’s *par excellence* collective action instrument. If the state is so strategic, its apparatus must be strong, sound, capacious and, for this very reason, its finances must be in balance. More than this, its debt must be small and long in maturity. The worst thing that can happen to a state as an organization (the state also stands for the rule of Law) is to be in thrall of creditors, be they domestic or foreign. Foreign creditors are particularly dangerous, as they may, at any time, leave the country with their capital. Domestic ones, however, transformed into rentiers and supported by the financial system, can impose disastrous economic policies on the country, as has been the case in Brazil.

**Chart 1: Old and new developmentalism, compared**

Old developmentalism	New developmentalism
State plays a leading role in terms of forced savings and investment in	State has a subsidiary, but important, role in both activities

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<sup>19</sup> See Bresser-Pereira and Dall’Acqua (1991).

firms	
Protectionist and pessimistic	Export-led and realistic
A certain fiscal lassitude	Fiscal discipline
A certain complacency towards inflation	No complacency towards inflation

The third and final difference between the developmentalism of the 1950s and new developmentalism can be found in the state’s role in promoting forced savings and investing in the economic infrastructure. Both forms of developmentalism cast the state in a leading role as regards assuring the proper operation of the market and providing general conditions for capital accumulation, such as education, health and transportation, communications and power infrastructures. In addition, however, under the developmentalism of the 1950s the state also played a crucial role in promoting forced savings, thereby contributing to countries’ primitive accumulation process; furthermore, the made direct investments in infrastructure and heavy industry, where the investments required were too high for the private sector’s savings.

This has changed since the 1980s. For the new developmentalism, the state still can and must promote forced savings and invest in certain strategic industries, but the national private sector now has the resources and managerial ability to perform a sizable portion of the investments needed. The new developmentalism rejects the neo-liberal thesis that ‘the state no longer has resources,’ because the state having resources or not depends on how its apparatus’s finances are managed. But the new developmentalism understands that, in all sectors where reasonable competition exists, the state must not be an investor, concentrating, instead, in defending and assuring competition. Even after these have been excluded, there are many investments left to the state, financed by public savings, rather than debt.

In sum, and again, in reflection of the different stage where medium development countries are at, new developmentalism regards the market as a more efficient institution, one more capable of coordinating the economic system, than did the old developmentalists although it is far from conventional orthodoxy’s irrational faith in the market.

#### 1.1.1.5 New developmentalism and conventional orthodoxy

Let us now examine the differences between new developmentalism and conventional orthodoxy. A conventional economic orthodoxy or conventional economic knowledge is made up of the set of theories, diagnoses and policy proposals rich nations offer developing countries. It is based on neo-classical economics, but not to be confused with it because it is not theoretical, but openly ideological and oriented towards proposing institutional reforms and economic policies. While neo-classical economics is based on universities, particularly in the US, conventional orthodoxy springs mainly from Washington, home to the United States Treasury Department and to the two agencies that are supposedly international, but in fact subordinate to the Treasury: the International Monetary Fund and the World Bank, the former charged with macroeconomic policy, the latter with development. Secondarily, it is originated in 'New York', that is, the seat or point of convergence of major international banks and multinationals. Therefore, we may say that conventional orthodoxy is the set of diagnoses and policies intended for developing countries and originating in Washington and New York. Conventional orthodoxy changes over time. Since the 1980s, it has become identified with the 'Washington Consensus', which cannot be understood simply as a list of 10 reforms or adjustments John Williamson wrote down on the *paper* that gave birth to the expression. His list even included reforms and adjustments that are indeed necessary.<sup>20</sup> The Washington Consensus is, in fact, the effective shape the neo-liberal and globalist ideology has taken at the level of economic policies recommended to developing countries. In some works, I distinguish between the First and Second Washington Consensus, to highlight that the former, materialized in Williamson's list, is concerned mostly with the macroeconomic adjustment that became needed as a result of the great debt crisis of the 1980s, while the second, prevalent since the 1990s, also intends to operate as a development strategy based on an open capital account and on growth with foreign savings. They form, however, a single consensus — that of rich nations in relation to their competitors, the medium development countries. Although the term Washington Consensus is useful, I prefer to conventional orthodoxy, because it is more generic and portrays a certain 'orthodoxy' as merely

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<sup>20</sup> Williamson (1990).

conventional.<sup>21</sup> Conventional orthodoxy is the means by which the United States, at the level of economic policies and institutions, express their ideological hegemony over the rest of the world, and mainly over dependent developing countries who lack nations strong enough to challenge this hegemony, as has been traditionally the case of Latin-American countries. This hegemony purports to be ‘benevolent’, while, in fact, it is the arm and mouth of neo-imperialism — that is, imperialism without (formal) colonies that established itself under the aegis of the United States and other rich nations after the classic colonial system ceased to exist, after World War II.

Inasmuch as conventional orthodoxy is the practical expression of the neo-liberal ideology, it is the ideology of the market vs. the state. While new developmentalism wants a strong state and a strong market, and sees no contradiction between them, conventional orthodoxy wishes to strengthen the market by weakening the state, as if the two institutions were party to a zero-sum game. Since the second half of the 20th Century, therefore, conventional orthodoxy has been a version of the *laissez faire* that prevailed in the previous century. Disregarding the fact that the state has grown in terms of tax load and of the level of market regulation as a result of the increased dimensions and complexity of modern societies, disregarding the fact that a strong and relatively large state is a requirement for a strong and competitive market, conventional orthodoxy is the practical reaction against the growth of the state’s apparatus. Certainly the state has also grown out of mere clientelism, to create jobs and employ the bureaucracy, but conventional orthodoxy is not interested in distinguishing legitimate state growth from the illegitimate. It is the ideology of the minimal state, of the police state, of the state that is concerned only with domestic and foreign security, leaving economic coordination, infrastructure investments and even social services like health and education to the devices of the market. It is the individualistic ideology that assumes all are equally capable of defending their interests. It is, therefore, a right-wing ideology, and ideology of the powerful, the rich, the better educated — the high bourgeoisie and the high techno-bureaucracy. Its goal is to

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<sup>21</sup> I have no sympathy for orthodoxy, which is a way to renounce thinking, and none for unorthodoxy where the economist, upon identifying himself as unorthodox, renounces seeing his ideas and policies in action, reserving himself the role of eternal minority opposition. A good economist is neither orthodox nor unorthodox, but pragmatic: he can make good economic policy based on an open, modest theory that forces him to constantly consider and decide under conditions of uncertainty.

drive down direct and indirect real wages by leaving labor unprotected, and, thus, making forms more competitive in an international market of developing countries and cheap labor.

The first and most general difference between new developmentalism and conventional orthodoxy was referred to in the foregoing section's final paragraph. Conventional orthodoxy is a market fundamentalist, believes that 'in the beginning there was the market,' an entity that coordinates all optimally as long as it is free, while new developmentalism holds no such beliefs. It regards the market as a remarkably efficient institution when it comes to coordinating economic systems, but is aware of the market's limitations. Factor allocation is the task it performs best, but even there problems arise. Incentives to investment and innovation leave much to be desired. And, at the level of income distribution, it is completely unsatisfactory a mechanism, as the markets privilege the strongest and most capable. While conventional orthodoxy does acknowledge the market's shortcomings, but argues that they are better than those of the state in attempting to correct them, new developmentalism rejects this pessimism towards the capacity for collective action and yearns for a strong state, not at the cost of the market, but in order for the market to be strong. If Man is capable of building institutions to regulate human actions, including the market itself, there is no reason why Man should not be able to strengthen the state as an apparatus or organization, making its rule more legitimate, its finances sounder, and its management more efficient; and to strengthen the state as a rule of law, making its institutions ever more closely aligned with social needs. This is precisely what politics and democracy are for.

As one of the bases for new developmentalism is classical economics, essentially a theory like Smith's 'wealth of nations', or Marx's 'capital accumulation', social structures and institutions are fundamental to it. In addition, as it embraces a historical perspective of development, the institutionalist teachings of the German historical school and of the American institutionalism of the early 20th Century are essential elements of its vision of development.<sup>22</sup> Institutions are, therefore, fundamental; and reforming them is a constant need inasmuch as, in

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<sup>22</sup> The German historical school is the school of Gustav Schmoller, Otto Rank, Max Weber, and, along a different path Friedrich List; the American institutionalist school is the school of Thorstein Veblen, Wesley Mitchell and John R. Commons.

our complex, dynamic societies, economic activities and the market must be constantly re-regulated. New developmentalism is, therefore, reformist. Conventional orthodoxy, on the other hand, based as it is on the neo-classical theory, has only recently become aware of the importance of institutions, with the emergence of the ‘new institutionalism’. Unlike historical institutionalism, which, at the level of economic development, regards pre-capitalist institutions and the distortions of capitalism as obstacles to development and tries to develop institutions to actively promote it, the new institutionalism is simplistic in its proposal: all institutions need to do is assure property and contracts or, more broadly, the proper operation of the markets, and the markets themselves will automatically promote development. In the neo-liberal jargon found, for example, in *The Economist*, a government is economically good if it is ‘reformist’ — where reformist means making market-oriented reforms. For new developmentalism, a government will be economically good if it is ‘developmentalist’ — if it promotes development and income distribution via the adoption of economic policies and institutional reforms oriented, as far as possible, towards the market, but often correcting these markets’ automatic actions. In other words, if it can rely on a national development strategy, for this is no more than this set of institutions and economic policies aimed at the proper operation of the markets and at development. For conventional orthodoxy, institutions must be almost exclusively limited to constitutional norms; for new developmentalism, economic policies and, more broadly, economic and monetary policy regimes, are institutions that require constant reform and adjustment within the framework of a more general strategy. Besides relatively permanent institutions, industrial policies are needed. They do not stand as a fundamental difference between new developmentalism and conventional orthodoxy, because new developmentalism uses industrial policy more moderately, topically and strategically, where the firm in need of support indicates that it has or will have the ability to compete internationally: an industrial policy that can be mistaken with protectionism is not acceptable.

Neo-developmentalism and conventional orthodoxy share many institutional reforms in common. But their objectives often differ. Take, for example, the public management reform. New developmentalism advocates it because it longs for a more capable and efficient state; conventional orthodoxy does so because it sees an opportunity to reduce the tax load. For new

developmentalism this may be a desirable consequence, but this is a different matter. The tax burden is a political issue that depends chiefly on the functions democratic societies assign the state and, secondly, on the efficiency of public services. In other cases it is a matter of quantity. New developmentalism favors trade openness, but is not radical about it, knowing how to use international talks to secure reciprocal advantages, since the world markets are far from being free. In other cases, it is a matter of emphasis: both new developmentalism and conventional orthodoxy favor more flexible labor markets, but new developmentalism, based mainly on experiences from Northern Europe, does not take flexibility for lack of protection, while conventional orthodoxy renders labor more flexible to make working conditions precarious and help push down wages.

#### 1.1.1.6 Two tripods, compared

In order to compare new developmentalism and conventional orthodoxy, let us examine the two pairs of tripods on which they are based: one pair of contradictory tripods concerned with development policy in general, and two pairs concerned with macroeconomic policy.

The development tripod of conventional orthodoxy can be stated thusly: “A country will develop propelled by the forces of the market, as long as: (1) it keeps inflation and public accounts under control; (2) it performs market-oriented microeconomic reforms; and (3) it obtains foreign savings to finance development, given the lack of local savings.” On the other hand, the tripod of new developmentalism states: “A country will develop by exploiting the forces of the market, as long as: (1) it maintains macroeconomic stability; (2) it can rely on general institutions that strengthen the state and the market and on a set of economic policies that stand as a national development strategy; and (3) it is capable of promoting domestic savings, investment and firm innovation.”

**Chart 2: Development tripods, compared**

<b>Orthodoxy</b>	<b>New developmentalism</b>
Control inflation and public accounts	Maintain macroeconomic stability

Reform to strengthen the market	Reform to strengthen the market and the state and have an industrial policy
Secure foreign savings	Promote domestic savings and innovation

I have already discussed item (2) of both tripods: for conventional orthodoxy, institutions are static; for new developmentalism, they are dynamic and make up a national development strategy. Let us now examine item (3). Item (1) will be discussed in the second pair of tripods, the one related to macroeconomic policy.

For conventional orthodoxy, the need for foreign savings is central. According to Washington and New York, developing countries will only achieve growth if they can rely on rich nations' capital. This is a central, unarguable point for conventional orthodoxy, it is a critical assumption. Quoth orthodoxy: 'it is natural for capital-rich nations to transfer their capitals to capital-poor countries. This vision has always been prevalent among economists and economic policy-makers of rich nations. In the 1970s, for the first time, foreign savings became abundantly available to developing countries. They took advantage of this 'opportunity' and the outcome was the great foreign debt crisis of the 1980s. In the early 1990s, when the foreign debt crisis was finally relatively resolved, a new wave of capital flows to developing countries begins, now within the framework of neo-liberal globalization, of openness not only in trade terms, but also of the capital account. In this context, Washington and New York do not dally but announce the new truth: 'no economic development is a great competition among developing countries to see who gets the most access to foreign savings.' The countries that most actively and faithfully dedicate to confidence building before their New York creditors and the Washington authorities, those that best follow their directions, will be those to achieve development, because they will benefit the most from foreign loans and direct investment.

New developmentalism rejects the notion that medium development countries need foreign savings to grow. And more: it understands that the strategy of growth with foreign

savings is the ideological stand-in for the law of comparative advantages in the process of neutralizing medium development countries' development. History teaches us that countries develop almost exclusively from domestic resources. At certain times, when investment opportunities are very large, current account deficits may beneficially speed up development, but these are exceptional circumstances. Normally, resorting to foreign savings, that is, to current account deficits, should be very restrained for two reasons. One is obvious: foreign debt can all too easily lead to balance of payments crises. And a more arcane reason, whose analysis has been the focus of my attention in the past few years: current account deficits are compatible with appreciated foreign exchange rates, artificially raising wages and consumption and reducing domestic savings, so that, ordinarily, when the expected rate of return is not particularly high, the inflow of foreign savings implies massive substitution of domestic with foreign savings. As a consequence, the country's development is little or none in the short term because of the capitals inflow and, in the meantime a burden is created in terms of debt and profits and interest remittance in the future, with a sure negative impact on growth.<sup>23</sup>

For conventional orthodoxy, chronic current account deficits and high foreign debt would be a 'natural' circumstance for developing countries; for new developmentalism, this is neither natural nor necessary, and the countries that develop the most — Asian countries — have been parsimonious in their use of foreign savings. They usually grow from foreign 'negative savings', that is, from current account surpluses. They receive direct investments, as do, by the way, rich nations, not to finance current account deficits, but, rather, as a reciprocation of investments abroad or increased reserves.

Macroeconomic policy also lies on two conflicting tripods. The conventional tripod argues that: "macroeconomic stability, understood essentially as control over inflation, is assured as long as: (1) the government controls its expenses, attaining a much-needed 'primary surplus;' (2) the sole purpose of the Central Bank is to control inflation, and its sole instrument is the interest rate, whose levels are not of import; and (3) the foreign exchange rate is floating within

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<sup>23</sup> I have been criticizing the growth with foreign savings strategy since the beginning of the decade. See, mainly, Bresser-Pereira (2002, 2004), Bresser-Pereira and Nakano (2002 [2003]), and Bresser-Pereira and Gala (2005).

the framework of an open capital account”. The neo-developmental macroeconomic tripod, in turn, argues that macroeconomic stability, understood to be inflation under control, moderate interest rates, and an exchange rate that assures foreign accounts’ intertemporal stability, will be attained as long as: (1) the government controls its expenses and public deficit, achieving positive public savings to finance its investments; (2) the Central Bank’s task is two-fold: to control inflation and to keep the balance of payments in balance; and it has two instruments: interest rates and foreign exchange rates; and (3) the foreign exchange rate is managed to remain competitive, using capital controls for this purpose when needed, and the interest rate remains as low as possible with stable prices.

**Chart 3: Macroeconomic tripods, compared**

<b>Orthodoxy</b>	<b>New developmentalism</b>
Get primary surplus	Get public savings
Central Bank with one task, one instrument	Central Bank with two tasks, two instruments
Open capital account and float exchange rate	Manage foreign exchange, using capital controls as needed

For both views, macroeconomic stability is fundamental to development, and fiscal discipline is essential to stability. But the differences begin with the definition of stability. Employment level is an essential element of true macroeconomic stability. The US legislation that regulates the Federal Reserve Bank, states that the Fed’s objectives are not only controlling inflation and keeping satisfactory employment levels, but provides a third variable: a ‘moderate’ interest rate. Both new developmentalism and conventional orthodoxy advocate firm control over public accounts, but, for conventional orthodoxy, the main metric is the primary surplus. The purpose of this is to make sure that the debt-to-GDP ratio does not increase and provide an assurance to debtors. New developmentalism is more ambitious: it wants to control public deficit

and, further, to achieve positive public savings capable of financing all, or a significant portion, of the public investments required.

While conventional orthodoxy defends a single Central Bank mandate — controlling inflation —, new developmentalism claims two mandates are needed: inflation and employment. While conventional orthodoxy sees no need for an upper limit to interest rates, new developmentalism wants monetary authorities to use their best efforts to keep interest rates low. Finally, a fundamental difference exists as regards the foreign exchange rate. For conventional orthodoxy, the market will deal with it, and, within the framework of a floating exchange rate, it is contradictory and counterproductive to try and manage it; for new developmentalism, this is the most strategic of all macroeconomic prices and, within reasonable limits or constraints, it can and must be managed. In order to manage the foreign exchange rate, the domestic interest rate has to be moderate, so as to allow purchasing reserves when capital inflows are too strong. At certain times, there may be a need to resort to capital controls. New developmentalism is in favor of these at the present time, along the lines of what Chile did in the 1990s.

Each one of the above points is deserving of a lengthy analysis, which, however, goes beyond the scope of this article. I do, however, note that the conventional macroeconomic tripod has strong influence from the growth with foreign savings strategy that became prevalent in the 1990s. Before, the IMF was concerned with foreign exchange rates and, during balance of payments crises, in addition to demanding fiscal adjustments, always demanded foreign exchange depreciations. Since the 1990s, however, the IMF forgot current account deficits (they were foreign savings, after all...) and exchange rate depreciations. The twin deficits hypothesis exempted it from worrying about current account deficits: all it had to do was concern itself with the primary surplus. For a while it chose to talk about foreign exchange anchors and dollarization; after the strategy failed in Mexico, in Brazil and, above all, in Argentina, the IMF turned to full-floating exchange to solve all external problems. The new developmentalism is strongly critical of this perspective and wants control not only over the state's public accounts (public deficit), but also over the nation's total accounts (current account); it wants not only the state's debt to be low, but also the state to show positive public savings; it also wants a nation-state to have foreign accounts that assure its national security and autonomy. It wants not only

interest rate management, but also foreign exchange rate management, even if within the framework of a floating rate regime that it does not call 'dirty', as conventional orthodoxy is wont to, but 'managed', instead.

#### 1.1.1.7 Conclusion

What are the results of the two policies? The outcome of conventional orthodoxy in Latin America is well known. Since 1990, at least, the truth from Washington and New York became hegemonic in this region marked by dependence. Reforms and adjustments of all sorts took place, but no development ensued. The results of new developmentalism in Latin America, in turn, cannot be measured. Chile has used it, but is a small country, and its policies are halfway between one strategy and the other. The Argentina of Kirschner and former Finance Minister Roberto Lavagna is the only concrete experiment, but far too recent to enable an objective appraisal. Still, new developmentalism is more than proven, because the strategy Asia's dynamic countries have been using is none other.

Can new developmentalism become hegemonic in Latin America as developmentalism was in the past? The conventional proposal's failure assures me that yes, it can. Argentina's 2001 crisis was a *turning point*: the requiem of conventional orthodoxy. No country was more faithful in the adoption of its prescriptions, no president was ever more dedicated to confidence building than Menen. The results are common knowledge. On the other hand, neo-developmental thinking is renewing itself. It has available a younger generation (as compared to my own or even Nakano's) of excellent economists that are graduating above all in Brazil. In Argentina and Chile too there are eminent economists that identify with this strategy, such as Osvaldo Sunkel, Aldo Ferrer, Ricardo French-Davis and Roberto Frenkel. There is, however, an issue of ideological hegemony to resolve. Latin American countries will only resume sustained development if their economists, businessmen and state bureaucracy recall the successful experience that old developmentalism was, and reveal themselves capable of taking a step ahead. They have already criticized the former mistakes, and realized the new historical facts that affect them. They must now acknowledge that the national revolution that was under way, with the old developmentalism as national strategy, was brought short by the great crisis of the 1980s and by the neo-liberal

ideological wave from the North. They must perform an in-depth diagnosis of the near-stagnation that conventional orthodoxy caused. They must turn an attentive eye towards the national development strategy of dynamic Asian countries. They must become involved in the great collective national work that is formulating the new developmentalism — the new national development strategy for their countries. I believe that this resumption of awareness is fully under way. Latin America's development has always been 'national-dependent' because its elites were always in conflict and ambiguous, now affirming themselves as a nation, now yielding to foreign ideological hegemony. There is a cyclical element to this process, however, and everything seems to indicate that the time of neo-liberalism and conventional orthodoxy has passed, and new perspectives are opening up to the region.

#### 1.1.1.8 References

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